[COMMITTEE PRINT]

THE CANADIAN ECONOMY AND ITS RELATIONSHIP TO THE UNITED STATES

COMMITTEE ON
BANKING, FINANCE AND URBAN AFFAIRS
HOUSE OF REPRESENTATIVES

95th Congress, Second Session

AUGUST 1978

Printed for the use of the
Committee on Banking, Finance and Urban Affairs

This report has not been officially adopted by the Committee on Banking, Finance and Urban Affairs and may not therefore necessarily reflect the views of its members.

U.S. GOVERNMENT PRINTING OFFICE
29–495 WASHINGTON : 1978

HOUSE COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

HENRY S. REUSS, Wisconsin, *Chairman*

THOMAS L. ASHLEY, Ohio
WILLIAM S. MOORHEAD, Pennsylvania
FERNAND J. ST GERMAIN, Rhode Island
HENRY B. GONZALEZ, Texas
JOSEPH G. MINISH, New Jersey
FRANK ANNUNZIO, Illinois
JAMES M. HANLEY, New York
PARREN J. MITCHELL, Maryland
WALTER E. FAUNTROY, District of Columbia
STEPHEN L. NEAL, North Carolina
JERRY M. PATTERSON, California
JAMES J. BLANCHARD, Michigan
CARROLL HUBBARD, Jr., Kentucky
JOHN J. LaFALCE, New York
GLADYS NOON SPELLMAN, Maryland
LES AUCOIN, Oregon
PAUL E. TSONGAS, Massachusetts
BUTLER DERRICK, South Carolina
MARK W. HANNAFORD, California
DAVID W. EVANS, Indiana
NORMAN E. D'AMOURS, New Hampshire
STANLEY N. LUNDINE, New York
EDWARD W. PATTISON, New York
JOHN J. CAVANAUGH, Nebraska
MARY ROSE OAKAR, Ohio
JIM MATTOX, Texas
BRUCE F. VENTO, Minnesota
DOUG BARNARD, Georgia
WES WATKINS, Oklahoma
ROBERT GARCIA, New York

J. WILLIAM STANTON, Ohio
GARRY BROWN, Michigan
CHALMERS P. WYLIE, Ohio
JOHN H. ROUSSELOT, California
STEWART B. McKINNEY, Connecticut
GEORGE HANSEN, Idaho
HENRY J. HYDE, Illinois
RICHARD KELLY, Florida
CHARLES E. GRASSLEY, Iowa
MILLICENT FENWICK, New Jersey
JIM LEACH, Iowa
NEWTON I. STEERS, Jr., Maryland
THOMAS B. EVANS, Jr., Delaware
BRUCE F. CAPUTO, New York
HAROLD C. HOLLENBECK, New Jersey
S. WILLIAM GREEN, New York

Paul Nelson, *Clerk and Staff Director*
Michael P. Flaherty, *Counsel*
Grasty Crews II, *Counsel*
Mercer L. Jackson, *Minority Staff Director*
Graham T. Northop, *Deputy Minority Staff Director*

LETTER OF TRANSMITTAL

To the Committee on Banking, Finance, and Urban Affairs:

Transmitted herewith for the use of the Committee on Banking, Finance and Urban Affairs is a committee print I have prepared.

Sincerely,

HENRY S. REUSS,
Chairman, Subcommittee on the City.

CONTENTS

Appendix

FOREWORD

As a native of a Great Lakes State, I have always had a friendly interest in this country's northern neighbor, Canada. Like many in the United States, I found part of the charm of Canada in the notion that that country was somehow a more pleasant, less crowded, less polluted version of the United States; speaking the same language, more or less; enjoying the same coast-to-coast diversity of a country as big as a continent. Also, like many of my countrymen, eventually I found that nothing so irritates Canadians as precisely that case of mistaken identity: the delusion that Canada is a smaller, even a "nicer" edition of the United States. Canada, they insist, is Canada.

So it is, and the pages that follow are designed to help members of the Committee on Banking, Finance and Urban Affairs sharpen their understanding of the Canadian qualities of the northern American continental economy as compared to our own southern American continental economy.

The origin of these pages is a visit to Washington by members of the Canadian House of Commons' Standing Committee on Finance, Trade and Economic Affairs last January. The Members of Parliament met with Government economists, academic economists, and, in the bipartisan spirit, economists of both the Brookings Institution and the American Enterprise Institute. One afternoon of their stay here, it was my privilege to preside at a luncheon meeting between the visitors and members of our own Committee on Banking, Finance and Urban Affairs. The discussion was lively, often highly pointed and always extremely instructive to the elected representatives of both nations. The chairman of the Canadian committee, Mr. Robert Kaplan, M.P., agreed with me that the exchange of views was profitable to both sides, and that the occasion should be repeated from time to time in the hope of furthering economic understanding among legislators whose committee work includes economic relations between the two nations.

This committee print has been researched and written toward the same end for the benefit, in the first place, of members of the House Banking, Finance and Urban Affairs Committee, of other Members of Congress and of the academic and general public interested in the question. Ms. Arlene Wilson of the Library of Congress Congressional Research Service, is the principal author. I commend her text to members for its lucid and concise exposition of a long, sometimes complicated history. A special feature is the appendix, in which are presented the details of the June 1978 breakdown of mutual fishing arrangements between the two countries.

In spite of that current concern, the history of economic relations between us is good. Our relations began, after all, with repeated efforts of the young United States to annex Canada by force. Certainly no sensible American has contemplated such adventures in well over a century.

Readers will perhaps be surprised, though they shouldn't be, that our two countries are each others' prime investors and prime customers; that for all intents and purposes there is a de facto common market in financial paper between New York, Toronto, and Montreal; that business, professional and trade associations are likewise held in common.

Obviously, it is premature even to think about a true and full common market between the two countries: the sheer size of the U.S. economy could not but seriously harm the Canadian in completely uncontrolled commerce. Nevertheless, we can and should look forward to increasing cooperation and to future action based on the recognition that our relationship is unique for both nations, is based on common ancestry and the common continental experience, and of its nature is mutually beneficial.

Henry S. Reuss,
Chairman

THE CANADIAN ECONOMY AND ITS RELATIONSHIP TO THE UNITED STATES

Introduction and Summary

INTRODUCTION

The purpose of this report is to provide a broad understanding of the current Canadian economy and how it has developed historically. No attempt is made to be all-inclusive; instead, only the most important influences are mentioned. Special emphasis is placed on the relationship between Canada and the United States.

This study begins with a brief discussion of the political and cultural influences in order to give a sense of perspective to the economic factors. Since Canada's economic development has been heavily influenced by the relationship among the provinces, a section on regional differences is included. The economic growth of Canada from 1775 to 1970 is outlined, followed by an analysis of the Canadian economy in the 1970's. Finally, the most important recent issues between the United States and Canada are discussed; these include problems and conflicts as well as areas in which considerable cooperation has existed.

SUMMARY

Political and cultural influences on the United States-Canadian relationship

Political conflicts between Canada and the United States were considerable in the first 80 years after the American Revolution. The United States invaded Canada twice and made inflammatory statements about annexing Canada from time to time. Although relations gradually improved, these U.S. actions probably still influence Canadians' feelings toward the United States. In the 20th century, Canadian-United States relations have been generally friendly, although many disagreements have emerged at times.

In terms of population and GNP, Canada is roughly one-tenth the size of the United States. This diversity of size has meant that U.S. policy decisions have had a large effect on the Canadian economy, but the reverse is not true, at least not until the energy crises of the 1970's. Canada's relatively small size, along with its geographical proximity to the United States, have contributed to her fear of political, cultural, and economic domination by the United States. Many attempts have been made to develop a unique cultural identity through national Canadian TV programs, films, and magazines, but the high cost of doing so has deterred some of these efforts. In addition, the lack of understanding and knowledge of Canadians by the U.S. Government and citizens irritates the Canadians.

29-495—78——2

Regionalism

Canada is composed of 10 Provinces—the original 4—Ontario, Quebec, New Brunswick, and Nova Scotia—which were united by confederation in 1867 and the other 6—Manitoba, British Columbia, Prince Edward Island, Saskatchewan, Alberta, and Newfoundland—which joined the Federation at a later date—plus the Yukon and Northwest Territories. At the time of the confederation, the Provinces were given subsidies based on need, and in turn, transferred their taxing powers to the Federal Government. These subsidies and tax powers have been a source of conflict ever since, and have been renegotiated many times, with the result that the provinces have greater tax powers today than they did earlier.

Income levels and rates of unemployment differ considerably among the Provinces; in recent years, Quebec and the Atlantic Provinces have grown more slowly than the other Provinces. Closeness to the large, buoyant Midwestern U.S. market has stimulated the economies of Ontario and the Prairie Provinces, while the increasing importance of scarce oil, natural gas, and other natural resources has benefited the Prairie Provinces.

Canada's geographically dispersed population has also added to conflicts over the customs tariff (favored by industrial Provinces such as Ontario but opposed by the Prairie Provinces), and the railroad rate structure, which favors industrial areas.

The separatist movement in Quebec has created considerable political and economic uncertainty. Reports abound of businesses and capital leaving Quebec for other Provinces or the United States because of the 1974 law making French the official language. Rene Levesque was elected Premier of Quebec in November 1976 on a platform of political separation from Canada, which, if it occurs, would cut off the Atlantic Provinces from the rest of Canada.

Economic growth of Canada

Canada's economic development has been heavily influenced by waves of immigration, railroad construction, the movement westward, and the growing demand for Canada's exports. After the U.S. Revolutionary War ended, the United States-Canadian boundary lines were mostly established and the first wave of immigration—40,000 British loyalists—took place, followed by another wave from the British Isles in the early 1800's. At this time, lumber, shipping, fishing, and agriculture were Canada's most important industries and the United Kingdom was her most important customer. In the middle of the 18th century, the old colonial system was replaced by free trade, and Canada's interest turned to the U.S. market. A 12-year reciprocal trade treaty between Canada and the United States was signed in 1854. This treaty lapsed in 1866 despite attempts to renegotiate it, and trade among the Canadian Provinces became more important. This potential trade, the necessity for a railroad linking the Provinces, and the political fear of a takeover by the United States after the Civil War made a union among the Provinces desirable. After confederation, which was achieved in 1867, a railway linking the east to the west was initiated (and completed in 1886), a high tariff was established to promote industrial development of the east, and agricultural development of the west was encouraged.

The Canadian economy was highly vigorous from 1896 to 1911, as more immigrants came from Europe and the United States and high world demand for wheat stimulated Canadian prosperity in other areas as well. After World War I, Canada's economy became primarily industrialized, with the pulp and paper, hydroelectric power and mining industries growing enormously, although agriculture was still very important, with wheat the leading crop.

Canada was especially hard hit by the depression of the 1930's; exports fell drastically, and a drop in wheat prices along with a drought made the Prairie Provinces the hardest hit of all.

A close military partnership between the United States and Canada developed during World War II and Canadian resources, and industrial capacity contributed heavily to the war effort. After the war, Canada was a major industrial power, and the discovery of oil, uranium, and iron further stimulated the Canadian economy, which entered a very prosperous phase.

The Canadian economy in the 1970's

The Canadian economy appears to have many problems in the late 1970's: Inflation and unemployment are both high, Canada's balance of payments has weakened and the Canadian dollar has depreciated substantially against the United States dollar in 1977 and 1978.

Although the 1974–75 worldwide recession was less severe in Canada than in the United States, Canada's economy since then has not exhibited sustained vigor as has that of the United States, despite a short-lived upturn in Canadian economic activity in late 1975 and early 1976. The rate of unemployment in Canada increased from 6.9 to 8.1 percent between 1975 and 1977, while in the United States it fell from 8.5 to 7.1 percent over the same period. From 1970 to 1975, monetary and fiscal policies were employed to mitigate the business cycle. Since then, however, Government policy has been directed at controlling inflation, considered to be the most important problem. Canada's inflation rate of 8 percent in 1977, high by historical standards, represents a decline from even higher rates in 1974 and 1975. This may be partially due to wage and price controls which were established by the Canadian Government in 1975 and removed in April 1978.

In the international sector, export growth has been small, partially on account of increased Canadian costs. Canadian tourism abroad and interest and dividend payments going abroad have increased. Direct investment by foreigners in Canada has declined, possibly because of lower expected profits and/or the Canadian Foreign Investment Review Act. In 1977, as a result of smaller borrowing requirement of the Provinces and the narrowing of the spread between Canadian and United States interest rates, new foreign borrowing declined.

For the above reasons, the Canadian dollar declined to a 45-year low of US $0.868 in April 1978. Also, it is possible that the Quebec uncertainties have stimulated adverse capital flows which contributed to the Canadian dollar depreciation.

United States-Canadian cooperation and conflicts in the 1970's

The energy crisis and environmental concerns have stimulated most of the disagreements that have occurred between Canada and the United States in recent years. Forecasts of Canadian energy resources have become increasingly pessimistic, which led to the Canadian

Government's cutting back on exports of oil and natural gas to the United States. In addition, an export tax was imposed on oil shipments to the United States, which was a source of irritation in the relationship between the two countries. Pipeline construction has also been part of the energy issue—in 1977, the United States and Canada ratified the transit pipeline agreement and, more importantly, an Alaska pipeline agreement was announced by President Carter and Prime Minister Trudeau in September 1977.

Environmental problems, such as water pollution and flooding—of waters—caused by dams, have usually been settled amicably, although sometimes after long discussion. Examples are the Great Lakes water quality agreement and the Garrison diversion project—currently under negotiation—which arose because the diversion of the Missouri River might increase the salinity of Canadian rivers.

The Canadian-American automotive agreement, signed in 1965, increased trade in automotive parts between the two countries from US$0.7 billion in 1964 to US$17 billion in 1976. Although some problems remain, the agreement has been beneficial to both Canada and the United States.

Direct investment by U.S. firms in Canada was welcomed by Canadians in the early postwar period, but by the later 1960's, many Canadians resented U.S. domination of their economy. The Foreign Investment Review Act, passed in 1973, restricts foreign investment to those that result in a "significant benefit" to Canada. However, most foreign investment applications have been approved since then, although the act may have deterred some foreign firms from applying.

The St. Lawrence Seaway, jointly constructed and operated by the United States and Canada, has been an enormous success. Occasionally, minor disagreements occur over the operation of the seaway, but they are amicably settled.

Political and Cultural Influences on the Canadian-United States Relationship

The economic relationship between Canada and the United States is only one part of a much larger relationship. Although the following discussion of the political and cultural aspects of the relationship is very brief, not only is an awareness of these factors essential for an understanding of the economic relationship between the two countries, but also these aspects are extremely important in their own right.

Political relations between the United States and Canada were quite hostile at the time of the U.S. Revolutionary War, but have gradually progressed to the generally friendly relations today. The occupation of Montreal and the attempted capture of Quebec in 1775 left the Canadians bewildered and angry at the United States. After the war, Benjamin Franklin suggested that "on the minds of the people in general, would it not have an excellent effect if Britain should voluntarily give up this province," [1] the first of several proposals for annexation of Canada by the United States made over the next century. After the War of 1812, during which the United States again invaded Canada, relations began to improve. Conflicts over the Oregon boundary and the Maine-New Brunswick boundary were settled in the 1840's. After the Canadian confederation in 1867, which was stimulated partly by fear of a political takeover by the United States, both countries were busy industrializing and moving westward, and problems were solved by mutual agreement.

From the 1930's through the 1960's, a close military and political partnership evolved—Canada not only actively participated in World War II, but also played a major role in the creation of NATO. In the mid-1970's Canadian politicians spoke of taking the so-called third option,[2] which referred to promoting ties with countries other than the United States and lessening Canada's dependence on the United States. At present, however, there is some evidence that the Canadian-United States relationship is improving, partially because, according to one observer, Canadians see the United States as "the ultimate security blanket if Canada starts to disintegrate." [3]

Although Canada is the seventh largest non-Communist country in the world in terms of GNP and second only to the U.S.S.R. in terms of geographic size, it is small relative to the United States in terms of population—23 million in 1977 compared with 217 million in the United States—GNP—U.S.$195 billion in 1977 compared with U.S.$1,890 billion in the United States—and military strength. This diversity of size is often assumed to be a large factor in the Canadian

---

[1] Tupper, Stanley R., and Douglas L. Bailey. "Canada and the United States—the Second Hundred Years." New York, Hawthorn Books, Inc. (1967), p. 16.

[2] The first option was continuation of the status quo, and the second option was increased ties with the United States.

[3] "A Wind of Change; Canadians Look South Again After a Period of Anti-Americanism." Wall Street Journal, Mar. 17, 1978, pp. 1, 27.

fear of domination by the United States. Until the energy crisis of the 1970's, Canada's actions have had relatively little effect on the United States. On the other hand, United States decisions often affect Canada to a considerable extent. The potential impact of United States actions on Canada, as well as the memory of the annexation attempts by the United States, has had an effect on Canada's feelings toward the United States.

While few Canadians seriously fear a political takeover by the United States, the threat of economic domination—and its consequent indirect political control—is felt by many people. Canadians sometimes feel, and there appears to be some justification, that the United States wants to dominate its economy, deplete its natural resources, and use it as a military buffer between the United States and the Soviet Union.

The Canadian desire to achieve its own cultural identity has been frustrated in part by U.S. dominance in Canada's communications industry. The fact that most of Canada's population lives within 100 miles of the U.S. border, combined with the economies of mass production in communications has exposed Canadians to U.S. radio and TV, films, and magazines to a considerable degree. The Canadian Broadcasting Corporation was established in the 1920's, partially to encourage production of Canadian programs, but high costs have resulted in the importation of more programs than was originally intended. In 1967, the Film Development Corp.—a Canadian firm—which provides financing for the private production of feature films, was established, but less than 2 percent of films shown on Canadian screens are of Canadian origin.[4] Also, in 1969, four out of five magazines read by Canadians originated in the United States.[5] In order to provide needed advertising revenues to Canadian-owned enterprises, the Canadian Government has made tax deductions available only for those advertising expenses paid to Canadian-owned TV stations and magazines. In retaliation, the U.S. Congress refused to exempt Canada from its 1976 law prohibiting tax deductions for more than two foreign conventions a year, which has hurt the Canadian convention business considerably.

Last but not least is the awareness or lack of awareness that Canadians and U.S. citizens have of each other. Canadian schoolchildren probably know more about the history and culture of the United States than adults in the United States know about Canada. U.S. citizens tend to regard Canada as an extension of the United States, partially because of the similarities in culture, history, religion, language, politics, literature, food, dress, and sports. Many U.S. citizens are largely uninformed about the Canadian identity; however, Canadians themselves are still in the process of defining that identity.

[4] English, H. Edward, ed. "Canada-United States Relations." New York Academy of Political Science, 1976. (Proceedings, v. 32, No. 2) p. 67.
[5] Ibid., p. 68.

Regionalism

Much has been written about Quebec's religious, cultural, and linguistic uniqueness, as well as about the separatist movement. Less well known are the differences among all of the other Provinces which have affected the Canadian economy as well as its relationship to the United States. These diversities relate to different income levels among the Provinces, geographic isolation, a long history of conflict in federal-provincial tax and expenditure relationships and conflict over rail transportation costs and customs tariff structures.

Four Canadian colonies—Ontario, Quebec, New Brunswick, and Nova Scotia—were united in 1867 when the British Parliament passed the British North America Act. The remaining six Provinces came into the Union at a later date—Manitoba in 1870, British Columbia in 1871, Prince Edward Island in 1873, Saskatchewan in 1905, Alberta in 1907, and Newfoundland in 1949. Nova Scotia, New Brunswick, Prince Edward Island, and Newfoundland are often referred to as the "Maritime" or "Atlantic" Provinces, while Alberta, Saskatchewan, and Manitoba are called the "Prairie" Provinces.

Other than the political fear of U.S. domination, the main motives behind confederation were economic. Increased trade among the colonies and with the United States, a stimulus to manufacturing activity, consolidation of debt—and better ability to borrow and finance railways and canals—were foremost among the objectives. In the process of reaching these objectives, the Provinces transferred their customs and excise tax collecting powers to the Federal Government, and in return received Federal subsidies, based on formulas which gave more money to the needy Provinces—subsidies were also given to those colonies and areas that joined the Dominion after confederation.

Many adjustments were made over the years in the subsidy formulas—later called equalization payments—in response to changing needs of the Provinces and claims of unfair treatment by the Provinces. Federal and Provincial taxing powers were also revised many times. Most of the changes in the past 30 years have shifted tax and expenditure powers to the Provinces and away from the Federal Government.

The main reason for subsidies and equalization payments is that the provinces differ greatly in terms of economic vigor, income levels, rate of unemployment, and so forth. In recent years, the economies of the Atlantic Provinces and Quebec have lagged behind those of the Prairie Provinces, Ontario and British Columbia, although in the 1800's the Atlantic Provinces were quite prosperous. Factors such as closeness to markets, resource base, industrial diversification and climate tend to cause this diversity. Ontario's closeness to the large, vibrant market of the Midwestern United States as well as the developed industrial structure of southern Ontario stimulates growth there. This compares with the Maritime Provinces, which are somewhat isolated from the main growth markets and whose comparative

advantage is concentrated in fish and coal. The Prairie Provinces have been most buoyant economically in the 1970's. Not only are Western U.S. markets large and growing but the increased importance of oil, gas, and other resources as well as higher resource prices, and the production of some staple goods which has moved west, have given the Prairies vastly increased prosperity and economic power.

In addition to equalization payments which even out income differences among the Provinces, in recent years an attempt has been made to stimulate employment in the weaker regions. In 1969 the Department of Regional Economic Expansion was created, which has been attempting to stimulate investment in new industry and expand basic investment needs such as roads and energy.

The geographic dispersion of the Canadian population over a wide area also tends to heighten regional conflicts. First, since the industrial, financial, government, and academic centers are mostly located in the region between Toronto and Montreal, people in the outlying areas of both the east and the west feel isolated. Second, the dependence of the Prairie Provinces on the railway has led to considerable conflict over transportation rates. Historically, rates have been based on a value-of-service principle whereby higher rates were charged those who needed the railroad most, instead of a cost-of-service principle. Inevitably, the Prairie Provinces, which depend on the rails to ship staples to markets and import consumption items, are hurt most by this policy.

Another source of contention is the high tariffs on Canadian industrial imports. This policy tends to discriminate against those Provinces that produce staples and import manufactured goods, which cost more than otherwise, while it favors those Provinces heavily engaged in manufacturing.

A recent Federal-Provincial conflict concerned the Federal export tax imposed on crude oil in 1973, which was later combined with a domestic price ceiling on the wellhead price of oil. This meant that the Provinces, which hold land or mineral leases on most of the land in which oil was extracted, lost a considerable amount of revenue.

In Quebec, regional differences are heightened by the fact that there are two cultures and languages represented in Canada. Although there are French-speaking people in all the Provinces, only in Quebec are the French concentrated and able to wield political power. Adding to the historical conflict of cultures is the fact that in the past 15 years, Quebec's relative economic position has deteriorated substantially. Although some analysts attribute this deterioration partly to language differences, economic factors such as the lack of investment—caused by fears of separation—are probably more important.

Some of Quebec's recent policy measures have alienated business firms and caused some firms to move or consider moving out of Quebec. In 1964, the Official Language Act, which makes French the official language of Quebec and requires business firms to undertake "francization" programs and make jobs available to French-speaking persons, was passed.[1] In January 1978, Sun Life Assurance Co. announced that it would move its head office to Toronto due to Quebec's Official Language Act. It is estimated that this proposed move would cost Quebec 1,800 jobs and $40 million annually.[2] In addition, recent per-

[1] English, H. Edward, ed. "Canada-United States Relations." New York Academy of Political Science, 1976. (Proceedings, v. 32, No. 2) p. 34.

[2] "Sun Life Assurance Company's Planned Move to Toronto." Canadian Press Comment, Jan. 25, 1978, No. 4 (Washington, D.C., Canadian Embassy), p. 1.

sonal tax revisions in Quebec have resulted in higher taxes on senior executives, which may increase the pressures for relocating elsewhere.[3]

In November 1976, the separatist movement led by Rene Levesque won election on the promise to seek political independence for Quebec while maintaining some sort of economic ties with the federation. Although the separatist movement has a long history in Quebec, the difference now is that it has gained political control. If separation does occur, the Atlantic Provinces would be cut off geographically from the rest of Canada, which would inevitably have some adverse effects on the Canadian economy and is the cause of considerable concern. Even the possibility of separation has probably led to adverse effects on Quebec's economy. Press reports have emphasized the moving of some Quebec residents and businesses to New York State and New England, as well as elsewhere in the United States, and people are reported to be transferring out of Quebec.

It is possible that the separatist movement in Quebec has contributed to increased contacts and perhaps closer relations between Canada and the United States.[4] Both factions are trying to obtain support in the United States; Prime Minister Trudeau and Quebec Premier Levesque make frequent speeches in the United States.

In addition to the 10 Provinces discussed above, Canada includes the Yukon and Northwest Territories, which account for more than 40 percent of Canada's land. Mining is the principal industry of the small population of Eskimos, Indians, and whites, while the fish and fur industries also provide some income to the population.

---

[3] "Quebec's Personal Tax Revisions Boost Pressure for Relocation of Head Offices." Wall Street Journal, May 8, 1978, p. 23.

[4] "A Wind of Change," pp. 1, 27.

29-495—78——3

Economic Growth of Canada, 1775–1970

Like that of the United States, Canada's economic development was spurred on by waves of immigration, the conquering of the frontier, railroad construction, and the process of industrialization. However, Canada's economy is more "open" in the sense that foreign trade and investment have played a far larger role in Canada than in the United States.

The U.S. Revolutionary War provided the first impetus to economic growth in Canada. Not only were boundary lines between the United States and Canada established for the most part, but about 40,000 British loyalists moved to Canada, most of whom settled in what later became New Brunswick and on the shores of the St. Lawrence River, and Lakes Ontario and Erie. Another wave of immigration took place in the first half of the 1800's; by 1850 Canada's population was over 2 million, compared with 500,000 in 1815. The immigrants, who were mostly from the British Isles, settled in Nova Scotia to work in the lumber, shipping, or fishing industries or New Brunswick's lumber industry, or went to what is now Ontario to farm or become tradesmen.

In the early 1800's, Canada's economy was more closely tied to that of the United Kingdom than the United States. The United Kingdom was Canada's largest customer because of tradition, the advantages of the colonial system with its preferential markets—colonial goods were admitted to Britain almost duty free, while other countries' goods faced a stiff British tariff—financial aid, and high U.S. tariffs. At this time, lumber in its various forms was Canada's chief export group, but wheat, furs, and fish were also very important.

As the old colonial system was replaced by free trade in the middle of the 19th century, Canada's interest in the U.S. market increased. Attempts to negotiate some form of reciprocal trade resulted in the signing of a 12-year treaty with the United States in 1854. This treaty provided for reciprocal free trade in coal and fish, farm and forest products. Also the United States gained access to inshore fisheries in a provision providing for U.S. access to the St. Lawrence and Canada's canals in exchange for Canadian access to Lake Michigan. In 1866 this treaty was allowed to lapse and although it was renegotiated several times in the next 50 years it was never approved by both the United States and Canadian governments.

The lapsing of the reciprocal trade treaty which made trade among the Provinces more desirable was one of several factors leading up to confederation in Canada. The U.S. Civil War had generated considerable tensions with Canada and the U.S. policy of "manifest destiny" in which U.S. expansionists talked of ruling the continent was a threat to Canadians. Perhaps more important was the Canadian realization that railroads were crucial to Canada's economic development. Although by 1860 there were 2,065 miles of track in Canada, many railroads went bankrupt and the lines were not linked to each other due to the lack of financial resources and political unity among the Provinces.

Confederation was realized in 1867 with the passage of the British North American Act joining together the four Provinces of Ontario, Quebec, New Brunswick, and Nova Scotia. Canada did not achieve complete independence from Great Britain in this act; for example, Canada could not negotiate with other countries and Canadian parliamentary procedures could be overruled by the British. However, the significance of this act was the opportunity it gave Canada to solve some of her problems, such as political, religious, and regional conflicts, economic isolation and stagnation.

After confederation, Prime Minister MacDonald's policy was threefold: A transcontinental railway to link the East and the West—which was completed in 1886—the agricultural development of the West, and the industrial development of the East. The latter objective was to be reached partially by the establishment of a high tariff wall, another of MacDonald's policies. From this time on, the tariff structure, although modified from time to time, has remained high, and often has been a controversial issue among the provinces. In general, the Maritime and Prairie Provinces opposed the tariff because it forced them to pay higher prices for consumer goods, while Ontario and Quebec, the industrial centers, were in favor of the tariff because it protected their own manufacturing industries.

From 1896 to 1911, Canada's economy entered a new, highly vigorous phase. Once again a flood of immigrants, this time from Europe as well as the United States, spurred on by the availability of Canadian land, was a stimulus to economic development. As world demand for wheat increased, wheat prices rose, and the Canadian prairies grew enormously, accompanied by prosperity in the rest of the country. For example, processed steel was produced in the Maritimes, while in Ontario and Quebec the thriving pulp and paper industry was joined by copper and silver extraction, along with production of a large variety of manufactured goods. British Columbia's lumber, mining and fishing industries prospered.[1] At the same time, a new railway boom was underway, which created thousands of new jobs and was an additional powerful stimulus to the economy.

World War I accelerated the growth of the economy as profits of both farmers and the producers of war supplies increased, as did the the demand for Canadian minerals. Canada, which along with the other dominions, signed the Treaty of Versailles herself and was given a seat in the League of Nations, had also entered into a period of greater political autonomy.

From the 1920's on, Canada was no longer primarily an agricultural country. In 1921, industrial production of $2.7 billion was almost double that of agricultural production, and the urban population of 4.4 million was about the same as the rural population.[2] Several industries in particular grew enormously—pulp and paper, hydroelectric power and mining. Agriculture was still very important, with wheat the leading crop, which stimulated a new railway boom. Economic development in the 1920's tended to proceed along regional lines, with the Maritime Provinces, which concentrated on fishing and lumbering, lagging behind the others.

---

[1] Lower, J. A. "Canadian History at a Glance." New York, Barnes & Noble, Inc., 1967 (c. 1966) p. 144.
[2] Ibid., p. 171.

The worldwide depression of the 1920's hit Canada particularly hard. Canadian exports fell drastically—export income fell by 67 percent between 1929 and 1933[3]—as nations reverted to high tariffs and import quotas to protect their own industries. Regional inequalities in the severity of the depression were apparent. A severe decline in wheat prices along with a drought made the Prairie Provinces the hardest hit of all. Those provinces which were heavily dependent on the export of primary products, such as British Columbia, the northern parts of Ontario and Quebec, also suffered sharp declines in income. Those areas engaged in manufacturing for the home market, such as the industrial regions of Ontario and Quebec, were the least hard hit.

During World War II, Canada's resources and industrial capacity were utilized to provide supplies for the Allies. Canada's transition to a major industrial nation was completed during this period. Trade between the United States and Canada was greatly stimulated by World War II, so that after the war the United States replaced Great Britain as Canada's chief customer.

After World War II ended, the discovery of oil in Alberta, of uranium in Saskatchewan and northern Ontario, and of iron ore in Quebec, provided the impetus for new industrial development as well as stimulating old industries. Population grew from 12 million in 1945 to 18 million in 1961, and 67 percent of the people lived in cities in 1956, up from 57 percent only 5 years earlier, due partially to the 2 million immigrants who came to Canada between 1945 and 1965.[4]

---

[3] Ibid., p. 176.
[4] Ibid., p. 205.

The Canadian Economy in the 1970's

Canada's economy appears to have many problems in the late 1970's—unemployment is high, inflation has hurt the Canadian economy, Canada's international trade position has weakened, and the Canadian dollar has depreciated against the U.S. dollar, reaching a 45-year low in April 1978.

Business cycles and unemployment

From 1971 to early 1974, Canada's economy was in a strong expansionary phase. Buoyant domestic demand, especially personal consumption expenditures, helped real GNP—dollar GNP adjusted for price changes—to grow by 6.6 percent in 1971, 5.6 percent in 1972, and 7.2 percent in 1973—see table 1. The worldwide recession of 1974–75 was less severe in Canada than in the United States—real GNP grew 3.2 percent in 1974 and 1.1 percent in 1975 in Canada compared with a decline of 1.6 and 1.3 percent in 1974 and 1975 in the United States. Domestic demand and especially residential construction after mid-1975 was stronger in Canada than in the United States, and the 1973–74 oil embargo affected Canada less severely than other countries. Also, vigorous fiscal and monetary policies were applied more quickly in Canada than in the United States. The international trade sector was the principal area of weakness in Canada over this period.

TABLE 1.—SELECTED ECONOMIC STATISTICS

	Annual growth rate in real GNP		Annual percentage change		Unemployment rate	
	United States	Canada	United States	Canada	United States	Canada
1970	−0.1	2.6	5.9	3.3	4.9	5.9
1971	2.9	6.6	4.3	2.9	5.9	6.4
1972	5.8	5.6	3.3	4.8	5.6	6.3
1973	5.4	7.2	6.2	7.6	4.9	5.6
1974	−1.6	3.2	11.0	10.9	5.6	5.5
1975	−1.3	1 1	9.1	10.8	8.5	6.9
1976	6.1	4.9	5.8	7.5	7.7	7.1
1977	5.0	2.6	6.5	8.0	7.1	8.1

Sources: OECD Main Economic Indicators, March 1978; OECD Main Economic Indicators, Historical Statistics, 1960–75; OECD Economic Outlook, December 1977; Bank of Canada Review, March 1978.

The surge in economic activity which began in mid-1975 lost momentum and the economy in 1976 was somewhat weak. GNP rose about 5 percent in 1976—of that, residential construction rose by 18 percent. The strength of the housing sector was partially due to Federal and Provincial policies, such as housing subsidies. In 1977, the Canadian economy grew by 2.6 percent, compared with the 5 percent growth of the U.S. economy.

The Canadian unemployment rate, which declined to 5.5 percent for 1974, has been rising every year since, reaching 8.1 percent in 1977, higher than the U.S. rate of 7.1 percent in that year. The labor force in Canada has grown rapidly, which, combined with sluggish economic growth, has caused the unemployment picture to worsen.

Wage and price increases

The rate of increase in consumer prices in Canada, as seen in table 1, has been high since 1973, both by historical standards and in comparison with the U.S. rate of inflation. It appears that the initial impetus to the inflation in 1973–74 came from exogenous factors, such as the rapid increases in world oil and food prices; the recent high rate of inflation, on the other hand, is probably due most to cost-push pressures, although food price increases were an important factor in 1977.

The high rate of inflation has stimulated unusually large wage and salary increases, particularly when measured against productivity increases. This has meant that unit labor costs have increased faster in Canada than in the United States from 1974 to 1976, which adversely affected Canada's competitive position.

Government policy

The Canadian Government has used monetary and fiscal policy actively in the 1970's to stimulate demand and to moderate the rate of inflation. In addition, wage and price controls were established in October 1975, in an attempt to mitigate inflation.

The annual budgets of the Federal Government have been the major fiscal policy tool. When restriction of demand is the aim, the budget is tightened, and when expansionary policy is desired to stimulate demand, taxes are reduced and expenditures increased. Timely countercyclical fiscal policy was applied in order to stimulate the economy in the early 1970's, to moderate demand in 1973, and stimulate demand in the recession of 1974–75. Since mid-1975, the main policy goal has been the reduction of inflation.

Monetary policy was also used in the early 1970's to stimulate the economy and since mid-1975 to reduce inflation. In the early 1970's the emphasis was on both the money supply and interest rates. In the past few years, however, monetary policy has been aimed mainly at controlling the growth of the money supply. This has led to relatively high short-term Canadian interest rates in 1975, for example, causing capital to flow to Canada. Consequently, the Canadian dollar appreciated in early 1976 even though the Canadian current account was in deficit.

The main goal of price and wage controls, which were established in October 1975, was to reduce the rate of increase in consumer prices gradually to 8 percent in the first year after controls, to 6 percent the second year, and 4 percent the third year. The controls were comprehensive, applying to prices, profits, wages, salaries, rents, dividends, and professional fees, and were quite detailed as well as flexible. Over the period of the controls, wages and price increases were lower than previously; however, it is unclear how much of the moderation is due to the controls. For example, from October 1975 to October 1976, import prices—which are an important factor in Canada's economy—rose only 1½ percent in Canadian dollar terms, and wage settlements were decelerating before the controls took effect. On the other hand, the controls may have contributed to a deceleration in price increases through their effect on expectations, and there is some evidence that wage compensation in the noncontrolled sector rose faster than in the regulated sector, indicating that controls had some influence. In any event, controls were very unpopular with the business community, and were removed in April 1978.

International trade and payments

An examination of table 2 below reveals the substantial deterioration in Canada's current account—net merchandise exports plus net service receipts plus net transfer receipts—in the 1970's from a small surplus in the early 1970's to a relatively large deficit in the latter part of the decade. This deterioration is due both to a narrowing of the merchandise trade surplus and an increase of the deficit in the services account.

There are two main factors in Canada's deteriorating merchandise trade position. First, business cycle swings in Canada and abroad—especially in the United States—have a large effect on Canada's exports and imports in the aggregate. Canadian exports are highly correlated with the level of economic activity abroad, while her imports depend on the level of domestic business activity. For example, in 1975, in the trough of a recession that was less severe in Canada than in the rest of the world, Canada's merchandise imports exceeded merchandise exports because her exports were hurt by the recession in other countries while her imports continued to increase substantially.

Second, the composition of Canada's trade has changed in the 1970's. Canada's trade balance in manufactured goods has deteriroated—both when automotive trade is included and when it is excluded from the data—which is probably caused by the increase in domestic costs. The oil and natural gas balance deteriorated because Canada is restricting exports as part of her energy program, and oil imports have been growing.

TABLE 2.—CURRENT ACCOUNT IN CANADA'S BALANCE OF PAYMENTS, 1970–77

[In billions of Canadian dollars]

	Merchandise exports	Merchandise imports	Net exports	Net services	Net transfers	Current account
1970	16.9	13.9	3.0	−2.1	0.2	1.1
1971	17.9	15.3	2.6	−2.4	.2	.4
1972	20.1	18.3	1.8	−2.5	.3	−.4
1973	25.5	22.7	2.8	−3.0	.3	.1
1974	32.6	30.9	1.7	−3.8	.6	−1.5
1975	33.4	34.0	−.6	−4.6	.4	−4.8
1976	38.0	36.9	1.1	−5.8	.5	−4.2
1977	44.6	41.7	2.9	−7.5	.4	−4.2

Source: Bank of Canada Review, March 1978, tables 68 and 69.

Two main factors have contributed to the worsening services account. First, Canadian tourist expenditures in the United States have increased considerably. Over most of the current decade, real disposable income in Canada has increased and consumer prices have grown faster in Canada than in the United States. Even after adjusting for changes in the exchange rate, it has been cheaper for Canadians to travel in the United States than at home. Second, the Canadian deficit on interest and dividend payments has increased substantially due to the increase in long-term interest rates and the high volume of borrowing abroad in recent years, most of which was by local and provincial Governments.

Direct investment in Canada by foreigners has been in a declining trend over the decade of the 1970's. This may be partially due to the

Foreign Investment Review Act, which may have led foreigners to feel unwelcome in Canadian industry, and/or partially to the high wage rates that must be paid in Canada and to the reduced profit potential. In contrast, direct investment abroad—especially in the United States—by Canadians appears to be an increasing trend, which again may be due to higher expected profit rates in the United States.

Most of the long-term Canadian borrowing abroad is done by provinces and corporations. Provincial Governments tend to borrow in the New York capital market because of their need for large bond issues which can only be absorbed by the large capital market of the United States. All new issues in 1977 are estimated to amount to C$6.2 billion, down from C$9 billion in 1976.[1] Two factors probably account for most of the decline—the smaller borrowing requirement of the provinces and the narrowing of the spread between Canadian and United States long-term interest rates.

The Canadian dollar

From 1971 through 1976, the Canadian dollar fluctuated around C$1 = US$1. In early 1977, however, the Canadian dollar began depreciating substantially against the United States dollar, reaching a 45-year low of C$1 = U.S.$0.868 in April 1978.

Most of the reasons for the depreciating Canadian dollar have already been discussed in earlier sections of this study. The large Canadian current account deficit of recent years—and the bleak outlook for an improvement in the current account in the near future—is one reason. Canada's weakened competitive position, as evidenced by relatively high wage and price increases, is another factor. Changes in capital flows—the lower direct investment by foreigners in Canada and decreased amounts of new bonds issued abroad discussed earlier—were also probably responsible for some of the depreciation. Not mentioned earlier was the narrowing of differentials between United States and Canadian short-term interest rates, which caused less short-term investment in Canada and more in the United States. Although difficult to substantiate, it is also possible that the uncertainties regarding the future of Quebec in the federation has contributed to the increased outflow of Canadian funds and the reduced inflow of United States funds, which may have put pressure on the Canadian dollar. In the spring of 1978, the Canadian Government announced that it was borrowing C$750 million in foreign markets, one of several measures aimed at supporting the Canadian dollar.

---

[1] Bank of Canada Review, March 1978, table 71.

United States-Canadian Cooperation and Conflicts in the 1970's

Since United States-Canadian differences tend to be solved by mutual agreement and conflicts sometimes arise in cooperative ventures, it is impossible to separate the two areas; therefore, cooperation and conflicts are discussed together.

Energy

In the field of energy, Canadian relationships with the United States are influenced by changing supply and demand conditions, regional considerations within Canada itself, the Canadian desire for increased economic independence and environmental concerns.

In the early 1970's, the outlook for Canadian energy supplies was bright. In 1971, the Minister of Energy, Mines and Resources stated that "Canadian soil contained sufficient reserves to supply gas for some 932 years and oil for about 390 years." [1] The supposed plentiful supply of oil and gas, as well as the fact that the price of exported oil was higher than that of imported oil encouraged exports in that period.

The 1973–74 energy crisis and increased price of imported oil stimulated new forecasts for future Canadian supplies, which were just the reverse of the earlier forecasts—quite pessimistic. For example, in October 1974, the Canadian National Energy Board announced that "Canadian oil supplies would not be adequate to serve traditional Canadian markets as well as part of the Montreal area beyond 1983." [2] As a result, export restrictions were imposed by the Canadian Government in which oil exports were to be gradually reduced to zero by 1983. In addition, an export tax on oil shipments to the United States was imposed, which created a two-price system and received a condemnatory resolution from the U.S. Senate. Not only did it raise oil prices to U.S. consumers—which probably would have happened anyway due to the rise in world prices—but it diverted oil company profits to the Canadian Government, which may have prevented some exploration and development by the oil companies. The receipts from this tax were used to subsidize oil imports into eastern Canada, which had the effect of not stimulating cutbacks in consumption.

Oil production is concentrated in the western part of Canada—the Province of Alberta accounts for 80 percent of Canada's oil production—while the eastern Provinces rely on imported oil. Due to the lack of a pipeline, oil is exported from the western Provinces and imported by the eastern Provinces, mostly from OPEC countries, especially from Venezuela. In an effort to become somewhat more self-

[1] Cestre, Ghislaine. "Petro-Canada: A National Oil Company in the Canadian Context." Washington, U.S. Government Printing Office, 1977, p. 5.

[2] U.S. Library of Congress. Foreign Affairs division. "The Current Canadian Situation" (prepared by Edward T. Lampson) Washington, 1975, p. 10.

sufficient, it was decided to extend the Ontario pipeline to Montreal—the extension was completed in 1976—and the 250,000 barrels per day that flow through this pipeline are at the expense of exports to the United States. This decision, and the decision to reduce oil exports to the United States, caused some hard feelings in the United States because the latter was not consulted first.

Canadian natural gas exports are based on long-term contracts, unlike oil exports, which are based on 30-day permits, a circumstance which makes it more difficult in the short term to reduce Canadian exports of natural gas than of oil. However, in 1975, it was decided to reduce Canadian gas exports due to a forecast that present gas production is inadequate to meet domestic requirements. However, the amount and timing of the decrease was to be decided after consultation with the U.S. authorities. Natural gas cutbacks are potentially more serious to the United States than oil cutbacks because gas transportation depends on the availability of pipelines. Also, the Canadian Government announced increases in the price of natural gas exports, a policy which is recognized by both Governments as being necessary, but the United States feels strongly that price increases should be gradual.

At the May 1977 meeting of the Canada-United States Interparliamentary Group, drilling in the Beaufort Sea was one of many energy issues discussed. It was decided that representatives of the drilling industry in Canada and the United States discuss technological problems further to insure environmental safety before permits were issued for drilling in the Beaufort Sea.

Considerable progress was made in 1977 on gas pipeline agreements. The United States-Canada Transit Pipeline Agreement, which provides protection against interference with the flow of natural gas in transit and against discriminatory tax policies of either country, was ratified by the United States and Canada. More important, perhaps, is the Alaska pipeline agreement announced by President Carter and Prime Minister Trudeau ln September 1977. After considerable study of the costs and environmental impacts of various routes for transporting Alaska natural gas to the United States, the ALCAN route was selected. Scme issues to be resolved in the ALCAN gas pipeline agreement include the pricing of gas, the pipe specifications, Provincial holdups, financing, the meaning of the "Canadian content" provision, and the possibility of delay through litigation.[3]

In early 1978, Vice President Mondale, on his trip to Canada, proposed a swap of Canadian-United States natural gas in which Canada would sell some of its current supplies to the United States in return for Canadian access to Alaskan gas later. Also, a United States-Canadian study is underway regarding the feasibility of a joint oil-storage facility in the Atlantic Provinces.

Environmental relations

Environmental concerns such as water pollution, air pollution, flooding of waters caused by dams and possible oil spills are inevitable

---

[3] Canada-United States Interparliamentary Group. Delegation from the United States. House Delegation. Nineteenth meeting of the Canada-United States Interparliamentary Group, Feb. 9–13, 1978; Report pursuant to Public Law 42, 86th Congress. Washington, U.S. Government Printing Office, 1978, p. 21.

in countries which share a long common border. In most of the controversial issues, the United States, which is more heavily industrialized and populated, receives both benefits and costs, while Canada may receive only social costs, such as increased pollution. Since the United States and Canada agree generally on the environmental standards to be met, conflicts have usually been settled amicably, although sometimes only after a considerable length of time. The existence of the International Joint Commission—established in 1909—with its impartiality and highly respected data gathering procedures, facilitated the settlement of many disagreements. The structure of Canadian Federal-Provincial relations, in which the Provinces have power in many areas, such as water and property rights that the United States do not have, tends to complicate settlement of some issues. The following paragraphs include a few of the recent and most important environmental concerns between the two countries.

The Great Lakes water quality agreement, which was signed in April 1972, provided for construction of municipal and industrial treatment plants within the Great Lakes system by both the United States and Canada. Some controversy arose over the speed of U.S. construction, but this is now settled. At the second round of negotiations in March 1978, substantial agreement was reached on a number of areas concerning the agreement.

The Garrison diversion issue refers to a project in which about 2 percent of the upper Missouri River would be diverted to eastern and central North Dakota for purposes of irrigation, flood control, water supply, recreation, and wildlife improvement.[4] Canadian objections arose because most of the drain-off of the irrigated lands with its high saline content will flow into Canada's Souris and Red Rivers. The International Joint Commission's report, which is currently being studied by agencies of the U.S. Government, recommended significant modifications of the Garrison diversion to prevent adverse effects in Canada.

An example of a coastal pollution issue is a U.S. company's 1972 proposal to build an oil refinery in Eastport, Maine, which would benefit New England. However, oil would have to be transported through Head Harbor passage—entirely in Canadian waters—which has serious navigation problems, such as fog and very strong currents. The possibility of an oil spill with its resulting damage to nearby fishing grounds and recreation areas caused Canadian objections to the project. At present the company is attempting to get U.S. approval to the proposal, and, if granted, will then consider Canadian concerns.

Foreign direct investment in Canada

As shown in table 3 below, foreign capital—most of which is U.S. capital—is a large share of all capital in Canadian industry, especially in the petroleum and natural gas industries. Foreign direct investment assumed a large role in the post-World War II period, and was welcomed by Canadians who perceived considerable advantages to the Canadian economy. In the past 10 to 15 years, however, many questions have emerged concerning the benefits to Canada.

[4] English, H. Edward, ed. "Canada-United States Relations," pp. 153–154.

TABLE 3.—UNITED STATES AND OTHER FOREIGN CAPITAL AS PERCENT OF TOTAL CAPITAL IN CANADIAN INDUSTRY, 1974[1]

Industry	United States	Other foreign
Petroleum and natural gas	58	17
Other mining and smelting	43	12
Manufacturing	44	14

[1] Capital in which there is voting control.

Source: English, H. Edward, ed., Canada-United States Relations, p. 76.

There are two main issues which apply to foreign direct investment in the petroleum, natural gas, mining and smelting industries. First, how should revenues be divided between foreign firms and Provincial governments—who own or have leases on most of the resource-producing land. Since the resource is on Canadian land, should not Canadian citizens benefit from some or all of the net gains involved in depleting the resource? Second, to what extent should prices, production, and investment in these industries be determined by Canadian governmental bodies in order to meet the national goal of conservation? The oil export tax and domestic subsidy on oil as well as the reductions in exports of oil and natural gas to the United States mentioned earlier in this study are examples of Canadian policies in this area which strained United States-Canadian relations.

The growth of foreign investment in the manufacturing sector was partially a free-market response to the high Canadian tariff structure—the only feasible way of gaining access to Canadian markets was to produce there. Many of the issues raised by foreign investment in this sector concern the power of multinational firms. One issue is the potential lack of competition among oligopolist multinationals and its effect on the Canadian economy. Another Canadian concern is the lack of an adequate flow of information between foreign firms and the Canadian Government.

Many multinational manufacturing firms are in industries where products are differentiated, such as soft drinks and soaps. This may have led Canadians to feel that they were being "sold" the American culture, which probably contributed to the mid-1970's feeling that the advantages of foreign direct investment may have been exceeded by its disadvantages.

The Foreign Investment Review Agency, which was established in 1973, was a reaction to Canadian dissatisfaction with foreign direct investment. This Agency has the power to review foreign-controlled firms' investment or takeovers of new businesses, while the Canadian Cabinet can accept or reject the Agency's recommendations. Only those takeovers that result in a "significant benefit" to Canada—based on a list of somewhat vague criteria, such as, for example, "compatability with industrial and economic policies"[5]—are to be approved. Since this policy has gone into effect, a large majority of the takeover applications have been approved. However, it is not known how many takeovers have been avoided by firms not even applying due to their expectation of being rejected.

[5] Ibid., p. 96.

Canadian-American automotive agreement

Before 1965, Canada's automotive industry, which was relatively inefficient in that output was too diversified for the limited size of the home market, was protected by high tariffs. Canadian measures were being proposed to increase home production by a duty-remission plan which might have invited retaliatory action by the United States. To prevent a potential conflict, bilateral negotiations with the United States were undertaken. These resulted in the Automotive Products Trade Agreement of 1965, which had the following three objectives:

1. The creation of a broader market for automotive products within which the full benefits of specialization and large-scale production can be achieved;
2. The liberalization of United States and Canadian automotive trade in respect to tariff barriers and other factors tending to impede it, with a view to enabling the industries of both countries to participate on a fair and equitable basis in the expanding total market of the two countries; and
3. The development of conditions in which market forces may operate effectively to attain the most economic pattern of investment, production, and trade.[6]

It was provided that the agreement may be terminated by either Government with 12 months' notice.

The implementation of the agreement centered on elimination of duties on trade in certain motor vehicles and original equipment parts in order to achieve a more integrated North American market. However, certain safeguards were imposed by each country. The Canadian safeguards, which were included to give industry time to adjust, were, in the view of the United States, intended to be temporary, and gave rise to U.S. dissatisfaction with the agreement at times.

Although some problems remain, the agreement has been beneficial to the United States and to Canada, but especially to Canada where it stimulated a large growth in output. Trade between the two countries increased from U.S.$0.7 billion in 1964 to U.S.$17 billion in 1976.[7] Canadian automotive production became more efficient relative to that of the United States resulting in considerable wage gains in Canada. Also, the differential in consumer prices paid by Canadian and United States consumers has narrowed in most years.

Prior to 1973, bilateral automotive trade resulted in a surplus for Canada—and a deficit for the United States—while since then a Canadian deficit (U.S. surplus) has existed. The U.S. surplus rose from $0.4 billion in 1973 to a high of $1.8 billion in 1975 and fell to $1 billion in 1976.[8] The 1975 surplus was partially caused by the 1974–75 recession, which was less severe in Canada than in the United States, resulting in higher Canadian imports from the United States and lower U.S. imports from Canada. However, Canadians are currently concerned that if present trends continue, the Canadian deficit could reach $2.5 billion by 1985.[9]

---

[6] U.S. Congress. Senate. Committee on Finance. Canadian Automobile Agreement. "Eleventh Annual Report of the President to the Congress on the Operation of the Automotive Products Trade Act of 1965." December 1977. Washington, U.S. Government Printing Office, 1977, pp. 2, 3.

[7] Ibid., p. 13.

[8] Ibid.

[9] Canada-United States Interparliamentary Group. Delegation from the United States. House Delegation. Nineteenth Meeting of the Canada-United States Interparliamentary Group, Feb. 9–13, 1978, p. 12.

The St. Lawrence Seaway

Discussion of a seaway by the United States and Canada had been underway since the 1930's, but had been opposed by U.S. rail and shipping interests and coastal ports who feared the competition. By 1951, when Canada began planning the seaway alone, the United States agreed to participate. The seaway was completed in 1959 and has been enormously successful in meeting transportation needs as well as stimulating economic growth in the midwestern parts of both countries.

The United States and Canada have differed on how to finance the operating deficit of the seaway. Since most of the locks are on the Canadian side, Canada was most concerned about the deficit, while the United States feared an increase in the tolls would divert traffic away from the seaway. However, both sides agreed that toll increases were necessary, and a new toll structure has been established beginning with the 1978 season.

Other

Private sector cooperation between Canada and the United States is the greatest of any two countries in the world. The large trade and investment flows—each country is the other's largest customer and largest direct investor—and the existence of a near common market in securities, loans, capital stock, and commercial paper between New York, Toronto, and Montreal attest to this cooperation. Also, business, professional, and technical associations are commonly operated jointly.

Recently, relations between the two countries seem to have improved. Vice President Mondale, who was given a warm welcome on his trip to Canada in January 1978, announced that the United States planned to ease the tax laws that have tended to keep U.S. convention business out of Canada. He also announced that the extraterritorial application of U.S. antitrust laws, another issue that had irritated Canadians, would be changed so that information would be sought voluntarily from subsidiaries of U.S. corporations and the Canadian Government would be consulted before court proceedings were utilized. In April 1978 a new interim agreement was reached on the fisheries dispute which arose from United States and Canadian 1976 laws extending sovereign jurisdiction 200 miles offshore. Currently new bilateral arrangements in energy resources, meat, and tourism are being negotiated.

Bibliography

BOOKS, PAMPHLETS, DOCUMENTS, ETC.

Bank of Canada Review. March 1978. 199 p.

Barrett, Charles A. Canada's international trade: trends and prospects. Ottawa, Conference Board, c1976. 55p. (Conference Board in Canada. Canadian studies, No. 39)

Canada. Department of External Affairs. Information Division. Facts on Canada. Ottawa, Queen's Printer, 1965. 43 p.

Canada-United States Interparliamentary Group. Delegation from the United States. House Delegation. Eighteenth meeting of the Canada-United States Interparliamentary Group, May 27–31, 1977; report by Dante B. Fascell, Chairman of the House of Representatives Delegation, pursuant to Public Law 42, 86th Cong. Washington, U.S. Government Printing Office, 1977. 19 p.

Canada-United States Interparliamentary Group. Delegation from the United States. House Delegation. Nineteenth meeting of the Canada-United States Interparliamentary Group, February 9–13, 1978; report pursuant to Public Law 42, 86th Cong. Washington, U.S. Government Printing Office 1978. 26 p.

Canadian-American Committee. A time of difficult transitions: Canada-U.S. relations in 1976; a staff report. Washington, 1976. 58 p.

Cestre, Ghislaine. Petro-Canada: a national oil company in the Canadian context. (95th Congress, 1st sess., Senate Committee on Energy and Natural Resources print) Washington, U.S. Government Printing Office, 1977. 65 p.

English, H. Edward, ed. Canada-United States relations. New York, Academy of Political Science, 1976. 180 p. (Proceedings, b. 32, No. 2)

Lower, J.A. Canadian history at a glance. New York, Barnes & Noble, 1967 (c1966) 248 p.

Maxwell, Judith, ed. Policy review and outlook, 1978: A time for realism. Quebec, D. C. Howe Research Institute, 1978. 157 p.

McNaught, Kenneth. The history of Canada. London, Heinemann Educational Books Ltd. (1970) 336 p.

Murphy, Lawrence J., et al. Perspectives on the Canadian economy: an analysis of cyclical instability and structural change. Ottawa, Conference Board, 1977. 100 p. (The Conference Board in Canada. Canadian technical paper No. 2).

OECD Economic outlook (No. 22) Paris, Organization for Economic Cooperation and Development, December 1977. 140 p.

OECD Main economic indicators. Historical statistics, 1960–75. Paris, Organization for Economic Cooperation and Development, 1976. 589 p.

OECD Main economic indicators. Paris, Organization for Economic Cooperation and Development, March 1978. 160 p.

Saywell, John. Canada past and present. Toronto, Clarke, Irwin & Co., Ltd. (1969) 64 p.

U.S. Congress. Senate. Committee on Finance. Canadian Automobile Agreement. Eleventh Annual Report of the President to the Congress on the operation of the Automotive Products Trade Act of 1965. December 1977. Washington, U.S. Government Printing Office, 1977. 80 p.

U.S. Library of Congress. Congressional Research Service. Alaskan natural gas: when and how (continuously updated) Issue Brief IB75083.

U.S. Library of Congress. Foreign Affairs Division. The current Canadian situation (Prepared by Edward T. Lampson). Washington, 1975. 13 p.

ARTICLES

Analysts see Canada foreign borrowing as just short-term aid to payments gap. Wall Street Journal, February 27, 1978, p. 7.

A wind of change; Canadians look south again after a period of anti-Americanism. Wall Street Journal, March 17, 1978, pp. 1, 17.

Canada section of gas pipeline faces high political hurdles. Journal of Commerce, February 6, 1978, p. 4.

Canada, U.S. map bilateral trade pact. Journal of Commerce. January 20, 1978, pp. 1, 15.
Hutchinson, Bruce. Canada's time of troubles. Foreign Affairs, v. 56. Oct., 1977, pp. 175–189.
Political problems draw Canada closer to U.S. Washington Post, January 23, 1978, p. A18.
Quebec's personal tax revisions boost pressure for relocation of head offices. Wall Street Journal, May 8, 1978, p. 23.
Quebec's separatist posture is a godsend to nearby States seeking firms and jobs. Wall Street Journal, March 14, 1978, p. 13.
Sun Life Assurance Company's planned move to Toronto. Canadian Press Comment. January 25, 1978, No. 4 (Washington, D.C., Canadian Embassy) 3 p.
United States-Canadian oil, fishing pact seen. Journal of Commerce. February 6, 1978, p. 32.

APENDIX

The June 1978 Fisheries Dispute Between the United States and Canada: A Résumé

Background

Fisheries disputes between the United States and Canada have erupted throughout the history of the two countries. The current dispute is the result of the extension by both countries of the fisheries jurisdiction from 12 miles to 200 miles in early 1977. This meant that some traditional fishing patterns of each country were disrupted because what were formerly international waters came under the jurisdiction of Canada or the United States. In 1977, a long-term agreement concerning maritime boundaries, salmon interception, and the management of east and west coast fisheries was being negotiated. But due to the complexity of the issues, a long-term agreement was not concluded and in order to allow traditional fishing patterns to continue, an interim agreement was reached in 1977. The most important provision of this agreement was that each country's commercial fishing could continue in accordance with existing patterns.

The Interim Reciprocal Fisheries Agreement for 1978

Since the long-term agreement was still pending when the 1977 interim agreement expired in December 1977, a new interim agreement was negotiated and subsequently completed on April 11, 1978. Besides retaining the provisions of the 1977 interim agreement, the 1978 agreement contained the following main additions:

1. Since the United States and Canada differ as to the length of chinook salmon that can be caught (the minimum U.S. size is 28 inches, while that of Canada is 26 inches), the United States agrees to allow Canadian salmon trolling vessels to carry chinook between 26 and 28 inches through the U.S. zone as long as the chinook were caught in the Canadian zone and the Canadian vessels report the number of such chinook to the U.S. authorities.

2. The area in which Canadian salmon troll fishing is allowed in the U.S. zone is larger than that permitted in 1977, subject to several conditions.

3. The United States has the right to request Canada to close the Swiftsure Bank area of British Columbia from April 15 through June 14, 1978, for conservation reasons (due to the number of immature salmon originating in rivers of the United States found in the Swiftsure Bank area). If Canada does not agree with the conservation need to close the Swiftsure Bank for this period, the United States is not obligated to permit Canadian salmon troll fishing in the agreed-upon expanded area nor to allow the carrying of 26- to 28-inch Canadian chinook through U.S. waters.

The Dispute

Disagreements over west coast salmon and east coast fish stocks led to the closing of United States and Canadian waters to reciprocal fishing on June 4. First, the United States requested that the Swiftsure

Bank be closed on April 14. Canada, not agreeing with the conservation need to close the bank, did not close it until May 15. Consequently, the United States did not grant Canada access to as large an extended area for salmon trolling in the U.S. zone as had been originally intended. In the meantime, the Washington State Trollers Association and the Quileute Indian Tribe obtained a temporary injunction on May 5 (which was stayed a few days later) barring all Canadian boats from trolling in U.S. waters, on the grounds that the Canadians didn't close the Swiftsure Bank when requested. In this court decision, the 1978 interim agreement was declared invalid because it lacked congressional approval.

The east coast fish stocks disagreement originated when Canada objected to efforts by U.S. fishermen to increase their catch of some fish stocks in the U.S. zone. The Canadians wanted these efforts to cease within a given time span, while the U.S. position was that under the 1978 interim agreement, the United States had no obligation to comply, and the legal steps necessary for compliance were impossible within the time limits set by the Canadians.

The inability to settle these two issues led to the June 2 note by the Government of Canada ceasing implementation of the 1978 interim agreement, with the resulting prohibition on U.S. fishing in Canadian waters effective noon, June 4. The United States took similar action, also closing U.S. waters to Canadian fishermen on June 4 (since a grace period was given by both countries to allow boats to leave the prohibited areas, reciprocal fishing actually ceased on June 6). In addition, the U.S. closed the Great Lakes to fishing by Canadians, although the Canadians did not extend their ban to the Great Lakes.

Legislation Concerning the Interim Reciprocal Fisheries Agreement for 1978

Due to the May 5 court decision mentioned above, congressional approval was required for the 1978 interim agreement. Consequently, legislation to approve the Interim Reciprocal Fisheries Agreement for 1978 was introduced in the House (H.R. 12571) and Senate (S. 3098). The House passed H.R. 12571 on May 25, 1978 and hearings on S. 3098 were held by the Senate Foreign Relations Committee on June 13, 1978, at which Mr. Lloyd Cutler, the chief U.S. negotiator of the 1978 interim agreement, recommended that the Senate complete the legislative approval of the 1978 interim agreement so that the executive branch would have the legal powers to resume negotiations concerning reciprocal fishing. During these hearings it was mentioned that the U.S. ban on Great Lakes fishing by Canadians was an "unintended complication" which had now been cleared up.

Other Factors Affecting Dispute

It is possible that the current fishing dispute has been complicated by feelings caused by previous as yet unresolved Canadian-United States disagreements. For example, at the June 13, hearing mentioned above, Mr. Jacob Dykstra, president of the Eastern Region of the National Federation of Fishermen, mentioned that Canadian subsidies to Canadian fishermen have adversely affected the U.S. scallop fishing on the Georges Bank. He also stated that U.S. fishermen felt that the United States is the side that usually grants most of the concessions in reciprocal fishery agreements.

Economic Impact

It is estimated that in 1977 the value of the U.S. fishery in Canadian waters and disputed boundary areas was $7.1 million and $15.7 million, respectively. Although the amounts involved are very small in relation to the size of the U.S. economy, the loss of these fisheries probably has a considerable adverse effect on some local economies as well as on the livelihood of the fishermen involved.

Other

Although at this writing reciprocal fishing remains prohibited, negotiations on the long-term reciprocal fisheries agreement between Mr. Lloyd Cutler, of the United States, and Mr. Marcel Cadieux, of Canada, are scheduled to resume June 19.

More detailed information on this topic can be obtained from the President's message to Congress on the Reciprocal Fisheries Agreement with Canada (H. Doc. 95–329), the report on the Fishery Conservation Zone Transition Act amendment (H.R. 12571) by the House Committee on Merchant Marine and Fisheries (H. Rept. 95–1215), and recent notes exchanged between the United States and Canada.

○